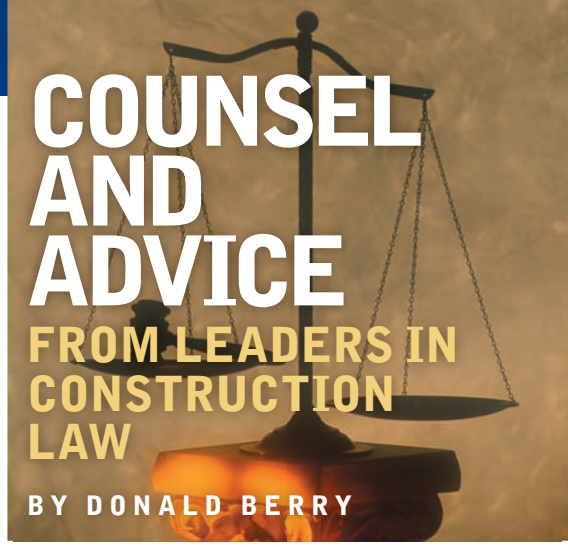
Executive Insights



COUNSEL AND ADVICE

FROM LEADERS IN CONSTRUCTION LAW

BY DONALD BERRY

Under the new Obama administration, Congress is expected to pass legislation to inject much needed capital into government projects. However, in the current economic climate, the construction industry landscape is a potential legal minefield and contractors should proceed with caution. In the words of Cozen O'Connor's F. Warren Jacoby, "With the high cost of litigation, few contractors can weather more than one significant claim, irrespective of whether or not they are liable."

How can you better position your construction company to successfully compete for projects in a tight market while effectively managing risk and reducing your exposure to claims? To find out, *Construction Executive* asked these leaders in construction law for their advice and counsel on a broad array of legal issues including insurance and bonding, cumulative impact, contract document disputes and, when litigation activity cannot be avoided, best practices to ensure your firm ends up on the winning side.

"What are common legal concerns for contractors in the area of insurance and bonding?"

F. WARREN JACOBY
Member and Chair, Construction Industry Practice
Cozen O'Connor

Historically, the process for the development of bids and proposals for projects has been relatively modular. On one hand, there is the need to properly identify the scope of work and the projected costs for same, while providing for contingencies such as weather, concealed conditions, other logistical issues, incomplete design, and so forth. In many cases, in addition to addressing protection for these exigencies in the pricing of the contract, the contractor could negotiate (although not always successfully) terms and conditions that may afford some level of protection with respect to these potential issues.

The second module for the contractor was risk management which until recently was a less significant facet in the planning stage. This had two forms, general liability insurance and surety bonding. However, depending upon the jurisdiction in which the contractor is located, the protection that had been historically provided by general liability insurance has been thrown in a cocked hat.

No longer do carriers provide indemnity and a defense for claims by owners relating to negligently performed work. Thus, even though contractors had for years expected this coverage to protect them when they are sued by owners relating to issues relating to the performance of their work, at the present time more and more jurisdictions have concluded that this coverage is no longer available under traditional general liability insurance, contending that this is the function of a performance bond—and not liability insurance. This has not only extended to coverage under the contractor's own insurance, but also to the insurance of their subcontractors where they are named as additional insureds. Further exacerbating this situation have been findings that not only deny indemnity and coverage to the contractor for damages to their own work, but extend that denial of coverage to claims for damages to other property.

Under this foreboding scenario, the contractor and its risk managers can no longer assume that their indemnity obligations and defense costs in the event of a problem with their work will be covered by the insurance premiums that they pay. The dilemma is substantial, especially given the competitive nature of the market and the thin margins. Moreover, as new insurance products and perceived risks evolve, including the fading of the fine line between contracting and professional construction management, the challenge of obtaining the right insurance coverage at a competitive price to protect the contractor is a greater challenge. And, in many instances, this is only exacerbated by the advent of OCIP and CCIP products, which present their own unique issues.

This situation is further compounded by the consolidation in the surety industry, resulting in fewer sureties, reduced limits, increased costs and increasingly more onerous bond provisions, from the standpoint of both the principal and the obligees. This not only dictates possible changed strategies to contractors in dealing with their owners and subcontractors, but places more pressure on the contractors in their selection of subcontractors and other vendors. Another development in this regard has been the advent of "subguard" like policies that have changed the traditional dynamic that has existed by and among the owner, contractor, subcontractors and sureties on projects.

Given the current economic climate, these pressing challenges need to be addressed by contractors, either individually, in conjunction with their advisors, or through their trade associations. With the high cost of litigation, particularly regarding electronic discovery, there are few contractors who can weather more than one significant claim, irrespective of whether or not they are liable. Otherwise, smaller and medium size contractors will become dinosaurs, with only large conglomerates able to self insure the risks presented by the constantly evolving insurance and bonding situation.